A. General Compensation Questions

What lessons have been learned from the research about personnel compensation in the private sector and how might these lessons apply to the development of new systems of educator compensation?

Many organizations, especially high-performance organizations, in the private and nonprofit sectors have, in recent years, developed new compensation strategies. A driving force behind the initiation of these strategies is the need to improve organizational productivity.

In the private sector, redesigned compensation strategies aim to mesh needed core knowledge and competencies with pay practices. Strategies include skill-based pay, competency-based pay, pay for knowledge, and collaborative rewards for adding value to performance. In such pay systems, individuals are not paid on the basis of length of service (seniority) or for doing a particular job. They are paid on the basis of the knowledge, skills, and competencies they use to accomplish new job tasks. Often, a portion of a team member's pay depends on the performance of the team as a whole (Odden & Kelley, 1997). In other words, organizations alter compensation structures to align organizational incentives and rewards with the strategic needs of the organization (Heneman & Von Hippel, 1995; Ledford, Lawler, & Mohrman, 1995).

Private industry often applies one of several theories of motivation to structure its employee compensation plans. Among the most often used theories are the following:

1. *Contingency Theory:* Incentive programs work when they fit with the basic strategies and characteristics of the organization. The more closely the incentive plan matches the overall vision of the organization, the more effective the plan is at motivating employees and increasing productivity (Lawler, 1990).
2. *Goal-Setting Theory:* Goals motivate employees when they are specific, challenging, accepted as worthwhile, and achievable. For incentive pay to be successful, it must be linked to these goals (Mohrman & Lawler, 1990; Mento, Steel, & Karren, 1987; Tubbs, 1986).
3. *Expectancy Theory:* People respond favorably to incentive programs if three conditions are met:
    - They believe they can accomplish the goal embedded in the incentive plan.
    - They believe there is a clear connection between individual effort and receiving a reward.
    - They value the reward enough to put forth the effort to achieve it (Heneman, 1992; Van Eerde & Thierry, 1996).

There is substantial evidence from the private sector that performance pay programs contribute to improved individual and organizational performance (Heneman & Gresham, 1998; Jenkins, Mitra, Gupta, & Shaw, 1998; Mitchell, Lewin, & Lawler, 1990). In fact, there is a large and sophisticated economics literature that is generally favorable toward performance incentives (see, for example, Baron & Kreps, 1999; Campbell, 2006; Lazear, 1998; Lazear, 2000; and Lazear, 2003; Prendergast, 1999).

Some research shows that applying the types of pay-for-performance plans typical in corporate America to the teaching profession could be successful. Lazear (2003), for example, proposes that increasing teacher pay and basing it on performance would substantially improve the overall quality of the teaching force. He contends that movement to a new compensation system that bases employee pay on outputs (e.g., measures of student performance) rather than inputs (e.g., experience and education) would have two effects. First, it would have a motivational effect on current teachers, encouraging them to change their practice in ways that will lead to higher levels of student learning. Second, movement to a new compensation system would have selection effects because it would attract a new pool of applicants and would retain high-performing teachers who fare well under it. Teachers who do not like the new system or who do not perform well under it would tend to self-select out.

Both Lazear (2003) and Podgursky and Springer (2007) emphasize the importance of selection effects. In a case study from the private sector, for example, Lazear (2000) found very large gains in productivity among installers of automobile windshields when their company switched to a performance-based pay system. Average levels of output per worker increased by roughly 44 percent. However, only about half of the gain in productivity was due to the average worker producing more because of incentive effects. The other half was due to an increase in average worker ability as a result of selection effects, i.e., hiring and retaining high-performing workers who are good at producing the desired output.

Podgursky and Springer (2007) examine other key findings from the economic research on performance incentives and suggest ways that these findings might apply to the development of new systems of teacher compensation. One frequently voiced concern about performance pay systems, for example, is that workers whose jobs involve multiple dimensions will direct their efforts toward those that are rewarded, which is a behavior economists term “multitasking” (Holmstrom & Milgrom, 1991). In the teaching profession, this could result in adverse consequences such as a narrowing of the curriculum or “teaching to the test.” Podgursky and Springer (2007) note that in the general personnel literature, the solution to multitasking is to use multiple measures of performance to determine rewards, such as principal evaluations of teacher performance in addition to student test scores.

Some evidence from economic research also suggests that workers are less likely to share information and to assist colleagues when they are competing for a fixed pool of limited funds (Drago & Garvey, 1998). Podgursky and Springer (2007) note that performance pay can be targeted to teams of teachers if concerns are strong that an individual performance pay program would be harmful to teacher collaboration. In addition, performance pay programs can be designed as open-ended systems rather than fixed-tournaments so that all teachers who meet specified performance targets are eligible for rewards.

Despite numerous positive reports about successful pay-for-performance systems, the private sector, as in the education sector, has had some less-than-successful experiences with merit pay. A number of industries and organizations have found that merit pay programs failed in situations in which: a) they were not strategic and did not connect with organizational mission and objectives; b) managers were unwilling (or unable) to conduct employee appraisals required of such programs adequately; c) they were poorly designed; and d) they were underfunded (Odden & Wallace, 2007).

Many private sector businesses moved away from strict merit programs in the 1980s and redirected pay-for-performance toward pay programs that rewarded employees for the acquisition and use of core competencies—or, stated another way, toward pay programs that focus on human capital rather than just on merit. They also directed portions of their pay programs to group-based incentives and adopted methods designed to attract and retain workers in "hot labor markets," which was the private sector equivalent to education's shortage fields (Odden & Wallace, 2007).

Evidence suggests that the implementation of performance pay programs may be nearly as important as their design in influencing program success and sustainability. Consultants involved with these programs (e.g., Orens & Elliott, 2002; McAdams, 1996; Gross & Bacher, 1993; Graham-Moore & Ross, 1990) consistently emphasize the importance of planning program implementation and ensuring execution according to plan. This concern is echoed by academics who have studied performance pay programs (e.g., Bartol & Locke, 2000; Heneman, 2002).

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